

Employer Stock: Fifth Third's Retention of Employer Stock Wasn't a Fiduciary Breach, Court Decides

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Fifth Third Bancorp did not breach its fiduciary duties by failing to divest its tax code Section 401(k) plans of Fifth Third stock during a time when the company was allegedly concealing its financial problems, the U.S. District Court for the Southern District of Ohio ruled Jan. 29 (*Shirk v. Fifth Third Bancorp*, S.D. Ohio, No. 05-cv-049, 1/29/09).

Magistrate Judge Timothy S. Black granted summary judgment in favor of Fifth Third as to claims by its employees that the company and its top officials breached their fiduciary duties under the Employee Retirement Income Security Act by retaining company stock as an investment option during a period when the stock was an allegedly imprudent investment.

The court found that the employees were unable to overcome the "presumption of prudence" that attaches to pension plans that invest in employer stock. According to the court, in order to overcome this presumption the employees would need to show not just that the stock value dropped, but that a reasonable fiduciary in the same circumstances would have made different investment decisions.

The court said that while the employees alleged that Fifth Third was "a complete and total mess" during the class period, this was insufficient as a matter of law to establish that a reasonable fiduciary in the same or similar circumstances would have divested the plan of Fifth Third stock.

The court's ruling disposes of all of the employees' "stock drop" claims challenging the inclusion of Fifth Third stock as investment options in the Section 401(k) plan. Left unresolved by the decision is the employees' claim that Fifth Third breached its ERISA fiduciary duties by "loading" its plan with several Fifth Third mutual funds that charged excessive and unreasonable fees. Last September, the district court denied Fifth Third's motion to dismiss the fees-related claim (192 PBD, 10/3/08; 35 BPR 2296, 10/7/08; 44 EBC 2936).

The Employees' Allegations

The employees alleged in their lawsuit that Fifth Third stock was an imprudent investment from Sept. 21, 2001, through April 7, 2004, because the plan's fiduciaries knew or should have known that the merger of Fifth Third with Old Kent Financial Corp. severely strained Fifth Third's infrastructure. This strain on Fifth Third's infrastructure eventually led the company to take an \$81 million pre-tax charge to reconcile erroneous accounting, according to the court.

The employees charged that Fifth Third and its top officials breached their duties by:

- offering Fifth Third stock as an investment option for the plans,
- providing incomplete and misleading information to plan participants regarding the prudence of investing in Fifth Third stock, and
- failing to appropriately monitor the plan's fiduciaries and provide them with accurate information about the company.

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In April 2007, the court denied Fifth Third's motion to dismiss the lawsuit. The court found in that decision that the employees had alleged adequately that Fifth Third and its directors breached their duties by engaging in numerous business practices that put Fifth Third stock at risk (70 PBD, 4/12/07; 34 BPR 920, 4/17/07; 40 EBC 2560).

Subsequently, the employees amended their complaint to add a claim that the company breached its fiduciary duties by "loading" its Section 401(k) plan with several Fifth Third mutual funds that charged excessive and unreasonable fees. Last September, the court denied Fifth Third's attempt to dismiss this fees-related claim.

Stock Fund Is an ESOP

In its most recent decision, the court granted the Fifth Third defendants' motion to dismiss all of the claims linked to the company's offering of its stock as an investment option.

As an initial matter, the court rejected the employees' contention that the plan's Fifth Third stock fund was not an employee stock ownership plan and as such was not entitled to the presumption of prudence that applies to plans that offer employer stock. The court found that the stock fund was an ESOP because an ESOP can form a portion of a Section 401(k) plan's investment options.

The court went on to reject the employees' argument that the presumption of prudence would not apply unless the plan documents actually "mandated" investment in company stock. The district court said the U.S. Court of Appeals for the Sixth Circuit does not condition application of the presumption of prudence on whether plan documents actually "mandate" investment in company stock.

According to the court, even if the presumption would apply only in situations where a plan mandated investment in company stock, in this case Fifth Third's plan actually mandated that Fifth Third stock be offered as an investment option. As such, the court found that the presumption of prudence applied.

Presumption Can't Be Overcome

The court then said that to overcome the presumption of prudence, it would not be enough for the employees to simply point to the drop in Fifth Third's stock value. "Rather, in order to rebut the presumption of reasonableness, Plaintiff must evidence that the circumstances would have prompted a reasonable fiduciary in the same ESOP circumstances to make different investment decisions," the court said.

The employees were unable to overcome the presumption of prudence, the court found, because they made no argument that a reasonable fiduciary in the same circumstance would have divested the plan of Fifth Third Stock. Among other things, the court noted that during the class period, institutional investors were increasing their holdings of Fifth Third stock and 50 percent of equity research analyst reports during the class period gave favorable outlooks to Fifth Third stock. The court said this type of evidence weighed against an argument that Fifth Third stock was an imprudent investment.

Moreover, the court found that Fifth Third's outside directors were not plan fiduciaries who could be sued by the employees. According to the court, the outside directors were not responsible for managing the plan's investments, nor did they have the authority to appoint the plan's fiduciaries.

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In addition, the court said Fifth Third did not breach its fiduciary duties by failing to disclose its financial situation to the employees. The court said the company would only have a duty to disclose "material" information about the plan, and the alleged internal control and risk management weaknesses experienced by Fifth Third was not the type of "material" information that needed to be disclosed to the employees.

The employees were represented by Geoffrey M. Johnson and Walter W. Noss of Scott + Scott, Cleveland Heights, Ohio; Beth A. Kaswan and Judith Scolnick of Scott + Scott, New York; and Amanda F. Lawrence and David R. Scott of Scott + Scott, Colchester, Conn.

The Fifth Third defendants were represented by Joseph M. Callow Jr., Jason M. Cohen, Danielle Marie D'Addesa, and Patrick F. Fisher of Keating, Muething & Klekamp, Cincinnati, and Patrick Michael Hagan, Victor A. Walton Jr., and Glenn Virgil Whitaker of Vorys Sater Seymour & Pease, Cincinnati.

The full text of the opinion is at <http://pub.bna.com/pbd/05cv049b.pdf>.